FORSYTH BARR

# FOCUS

SPECIAL REPORT

FRIDAY 8 MAY 2020

# Trade War 2.0

**Although Covid-19 dominates the headlines, the US Presidential election, due November 3rd, creeps closer. The election looked tight before the Virus Crisis. Now it's on a knife edge. A tight race and rebounding share market may tempt President Trump to reignite a trade confrontation with China to, amongst other things, emphasise his global heft to voters.**

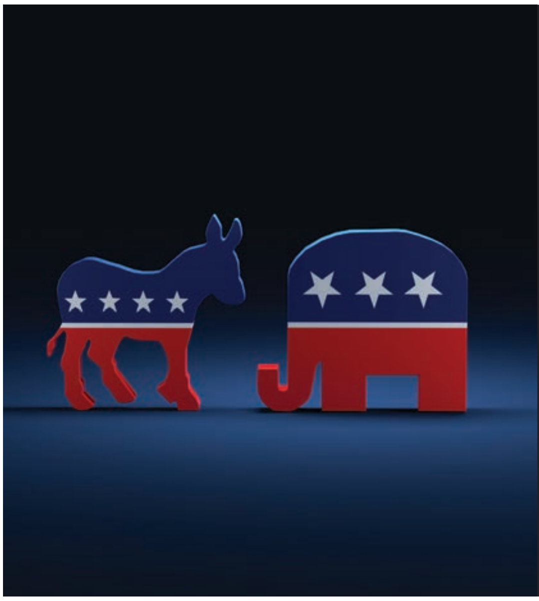
Are tougher times for investors likely to make a comeback? Possibly. The relief of emerging from Covid-19 may prove short-lived, as Sino-US geopolitical tension intensifies ahead of November 3rd.

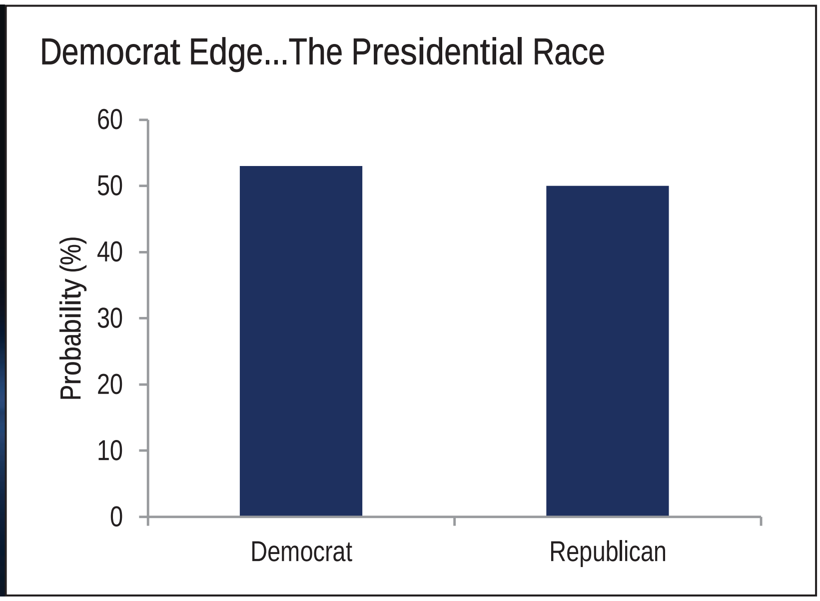
## Key Points To Consider

- New Zealand continues to prepare for a step back from the most extreme lockdown measures imposed through March/April. From there, we expect the economic focus to turn to a clean-up of the damage wrought.
- Data has begun to flow on the state of the US labour market. As a rule of thumb, the decimal place has shifted to the right. Weekly jobless claims number in the millions, rather than the hundreds of thousands. The unemployment rate will likely move into double digits this weekend. How long the environment remains this dire depends on the duration of the lockdown. One positive is that numerous States have begun planning to ease social distancing measures.
- Any return to “normalcy” will have a potential sting in the tail. November 3 brings the US Presidential election. President Trump will not have a buoyant economy to float him into a second term. Rebounding markets may embolden the self-styled “Tariff Man” to reignite hostilities with China. Ironically, one thing in investors’ favour is the fragile state of the US economy, which may restrain the President.

## Knife Edge Politics

As the US Presidential election, due November 3rd, creeps closer, there is increasing focus on the decreasing margin between the two major political parties. The Democrats hold a slim lead in prediction markets (below), but this has fluctuated and the election remains too close to call.






Source: Predict It, Forsyth Barr Analysis

A tight race and rebounding share market may tempt President Trump to reignite a trade confrontation with China to, amongst other things, emphasise his global heft to voters. Indeed, last Sunday, the President made some of his strongest comments for some time. Referring to China’s January agreement to buy additional US exports, Trump said, “They took advantage of our country. Now they have to buy and, if they don’t buy, we will terminate the deal. Very simple.”

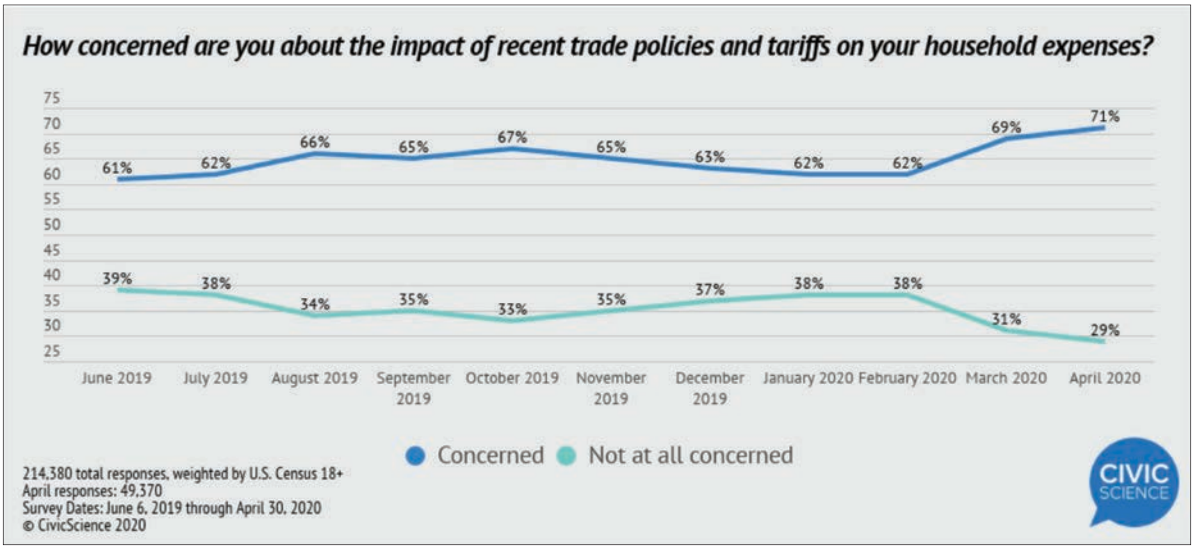
Secretary of State Mike Pompeo has been even more inflammatory, claiming “enormous evidence” that Covid-19 originated from a Wuhan laboratory.

Irrespective of whether this allegation has legs, the backdrop of US-China relations has soured materially from the January signing of a Phase One trade deal.

## Tariffs Matter

Tariffs matter for markets. In 2018 when the Trade War moved from talk to action, shares in the US were down for the year, including a nasty sell-off in the fourth quarter. To be sure, the primary reason for the almost 20% decline from September through December was rising interest rates. But the trade dispute meant investor sentiment was brittle to start with.

US consumers are worried about tariffs. A recent survey showed an increasing awareness of the impact of trade conflict on household budgets (below). US consumers are dealing with some of the harshest conditions in many decades. A fresh trade dispute will test frayed resilience.




## Trump, Fettered

It is possible that there are tougher times for investors ahead. Intensifying Sino-US geopolitical tension ahead of November 3rd, could mean that the relief of emerging from Covid-19 may prove short-lived.

Against that, there are sound reasons for expecting President Trump to tread carefully in the election campaign:

- First and foremost, Trump will want voters to at least believe the economy is recovering come Election Day. A full-blown trade war with China would disrupt that narrative.
- Secondly, notwithstanding Covid-19 questions, there has been a trade agreement signed. This creates a basis for dialogue that didn't exist in 2018.
- Finally, the timeline (less than 6 months), should limit the scope for sweeping measures. Even hasty trade policy takes time.


Nevertheless, President Trump's recent comments are a reminder that Covid-19 is not the only driver of markets. We will be parsing Presidential language with watchful interest as November nears.

Given the importance of the US to the global economy and financial markets generally, all investors will need to carefully consider trends in the US economy as part of their overall portfolio considerations. Leveraging our global research relationships, your Forsyth Barr investment adviser is well-equipped to provide you with the insight necessary to ensure your investment portfolio is appropriately positioned in the current environment.

***Stay well and we look forward to the next easing of the lockdown.***

**Bernard Doyle**
Head of Portfolio Advisory Group

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**We have begun producing short videos to provide snapshots of key market topics. These will include regular market updates, along with analysis of individual stocks and sectors (this week they include an overview of Quantitative Easing and an update on the Retail Sector). You can find these video updates in the Research Video insights section of the website here. https://www.forsythbarr.co.nz/research-library/research-video-insights/**